MAXUS EXPLORATION CO.

IBLA 94-732 Decided August 27, 1997

Appeal from a June 27, 1994, Decision of the Deputy State Director, Utah State Office, Bureau of Land Management, affirming the April 25, 1994, Decision of the Vernal Associate District Manager, concluding that 324,323 Mcf of vented gas was avoidably lost during the period January 1, 1978, through December 31, 1983, from various leases then held by Diamond Shamrock Exploration Company (now Maxus Exploration Company). Lease Nos. U-017985, U-017992, U-020252-A, U-3563-A, and U-7978.

Reversed in part, set aside in part, and remanded.

1. Administrative Authority: Generally--Oil and Gas Leases: Generally--Oil and Gas Leases: Royalties: Generally

   When evidence that there are engineering, geologic, or economic reasons to justify venting or flaring gas from oil wells has been presented to BLM by a lessee who appeals from a decision that there has been avoidable waste as a result of such venting or flaring, this information must be considered.

2. Administrative Authority: Generally--Oil and Gas Leases: Generally--Oil and Gas Leases: Royalties: Generally

   Proper application of Instruction Memorandum No. 87-652 required that BLM evaluate whether, if an application to flare gas had been made for oil wells produced by the lessee prior to flaring, the application would have been entitled to approval on the merits.

3. Oil and Gas Leases: Generally--Oil and Gas Leases: Royalties: Payments

   A finding that a lessee must pay the United States for the full value of vented gas that was avoidably lost from 1980 to 1984 is reversed, because 43 C.F.R. § 3162.7-1(d), issued in October 1984, changed Departmental policy to require that compensation for avoidably lost gas shall be limited to payment of the royalty value of gas so vented. Because the 1984 regulation changed the prior policy, which had been to assess vented gas at full value, affected lessees who would benefit by the amended rule are allowed the benefit of the change.

4. Administrative Authority: Generally--Appeals: Jurisdiction--Board of Land Appeals--Judicial Review

A statute establishing time limitations for commencement of civil actions for damages by the United States does not apply to limit administrative review within the Department of the Interior.

APPEARANCES: Michael J. Wozniak, Esq., Denver, Colorado, for Appellant.

OPINION BY ADMINISTRATIVE JUDGE TERRY

Maxus Exploration Company (Maxus), successor to Diamond Shamrock Exploration Company (Diamond Shamrock), has appealed from a June 27, 1994, Decision of the Deputy State Director, Mineral Resources, Utah State Office, Bureau of Land Management (BLM), that affirmed the April 25, 1994, Decision of the Vernal Associate District Manager (ADM), concluding that 324,323 thousand cubic feet (Mcf) of gas vented during the period January 1, 1978, through December 31, 1983, from various leases then held by Diamond Shamrock was avoidably lost.

This appeal is the culmination of a review that began in late 1983, when Minerals Management Service (MMS) initiated an audit of Federal royalty payments made by Maxus. On February 20, 1985, the Tulsa Regional Compliance Office, MMS, issued a Decision assessing 100 percent compensation based upon the full ceiling price of natural gas that was allegedly vented and flared from 15 separate Federal leases operated by Maxus' predecessor, Diamond Shamrock (5 of which are the subject of this appeal). The MMS claimed that this compensation was due, based upon 30 C.F.R. § 206.100 and implementing regulations. Maxus appealed, claiming that no "waste" had occurred because venting and flaring were justified by economic conditions, geological conditions and physical characteristics of the remote properties, the combination of which rendered compliance with production alternatives listed in the regulations impossible. Maxus challenged the 100 percent penalty assessment as well as the ceiling price valuations relied upon by the MMS. All the wells in the five leases subject to this appeal were producing oil wells located in remote areas not initially possessing access to gas gathering infrastructure.

On October 16, 1987, MMS issued a Decision on the Maxus appeal. The MMS Decision remanded the Maxus appeal to the Royalty Management Program for recalculation of royalties and assessments after BLM determined, pursuant to the policies established by BLM Instruction Memorandum (IM) No. 87-652, issued August 17, 1987, whether Maxus must pay the full value of gas, the royalty value, or nothing.

In the April 25, 1994, Decision issued by the ADM for Mineral Resources, Vernal District, BLM, Maxus was advised that BLM IM No. 87-652 supported full value assessment for 324,323 Mcf of natural gas determined to be avoidably lost during the 1978-83 period. Maxus was advised that, should it desire to dispute this determination, it could request a State Director review. Maxus sought State Director review.

The June 27, 1994, Decision by the Deputy State Director, BLM, Utah State Office, held:

> Bureau policy concerning avoidably lost gas is contained in Instruction Memorandum No. (IM) 92-91, dated January 3, 1992 (copy attached) which replaced the previously issued IM 87-652. The BLM's policy remains that gas produced from or allocable to a Federal lease may not be vented or flared absent the authorized officer's prior written approval. The review procedures within IM 92-91 are the same as those contained in IM 87-652, modified to adopt the Interior Board of Land Appeals decision in Mobil Exploration & Producing U.S., Inc. (119 IBLA 76, [98 Interior Dec. 207,] April 5, 1991) and to update the previous instructions as a result of events which occurred after the issuance of IM 87-652. However, other than the royalty value issue, the procedural updates would not have affected this decision under review.
>
> Under IM 92-91, where the operator fails to obtain prior approval to vent gas, but later captures the gas for sales, the volume of gas vented from the end of the initial 30 day test period until the time of capture is considered avoidably lost, without regard to the economic circumstances. Royalty is due on that same volume of gas. The ADM reviewed the situation on the five involved Federal leases which were operated by Diamond Shamrock Exploration Company (later known as Maxus Exploration Company, now known as Maxus Energy Company), and appropriately determined that venting occurred without prior approval, that the gas was later captured, and that an avoidable loss had occurred.
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> The amount of gas that was vented without approval is also under review. The volumes were taken directly from Monthly Reports of Operations (MRO) submitted by the operator. In those situations where Bureau MRO data was absent or questionable, information was utilized from State of Utah Monthly Production Reports or recent discussions with the operator. Each of the monthly gas production values, the initial authorized test values, the "used on lease" values, and the resultant gas vented values were verified as correct by this office.
>
> Therefore, the decision of the ADM that gas vented was avoidably lost and the total vented volume of 324,323 [Mcf] is hereby upheld.

Royalty value, to be established by the Mineral Management Service, is due on the avoidably lost gas.

(Decision at 1-2 (emphasis provided).)

In its appeal to this Board, Maxus argues that the above quoted interpretation of IM No. 87-652 and its successor IM No. 92-91 are clearly wrong and inconsistent with decisions of this Board. (Statement of Reasons (SOR) at 11.)

Maxus first establishes the following facts, which were also presented in its earlier appeal to BLM: (1) Maxus' production occurred in a remote area having no pipeline infrastructure; (2) All Maxus' wells were oil wells which incidentally produced casinghead gas; (3) The reservoirs from which the wells produce are solution gas driven reservoirs which do not lend themselves to shut-in of incidentally produced gas without damaging the reservoir and oil productivity; (4) The United States Geological Survey and BLM were aware of Maxus' venting activity on these leases, had a nearby adjacent office, had frequent communication with Maxus, made numerous inspections of these wells, and were fully aware of Maxus' plans and operational endeavors, yet they never objected to Maxus' venting; (5) Monthly reports which evidenced the venting were filed for years without any objection by BLM; (6) Maxus was ordered to drill and complete a well on Lease U-3563-A to prevent possible drainage and BLM had full knowledge that no pipeline infrastructure existed and the gas would not be captured; (7) The only pipeline infrastructure was the Mountain Fuel pipeline; (8) Prior to when these wells were ultimately connected, Mountain Fuel refused to buy casinghead gas; (9) Due to the Mountain Fuel refusal to buy this gas, it would have cost Maxus millions of dollars to build a gathering system, compression system and intrastate pipeline transportation system to transport this incidental volume of casinghead gas to a market; (10) When Mountain Fuel was persuaded to purchase casinghead gas (with a "high-take" obligation) from Maxus, Maxus immediately (within 90 days) spent $1.4 million to build the necessary gathering compression system to connect to the Mountain Fuel interstate pipeline system; (11) The total operations on the lease clearly justified, on any economic basis, production of the oil and paying the oil royalties while venting the incidental casinghead gas; and (12) It remained uncertain as late as the date that Maxus sold its interest in these entire fields whether its gathering investment to capture this gas would prove to be economic. (SOR at 11-13.)

In its appeal, Maxus claims that there has been no review or analysis of any of the economic evidence it submitted. Rather, Appellant submits, the Utah BLM automatically applied an interpretation of IM No. 87-652 and IM No. 92-91 that nothing would justify casinghead venting if a subsequent connection occurs. Appellant further submits that, to the extent that IM No. 87-652 and IM No. 92-91 are applicable, the interpretation adopted by BLM contradicts the goal, purpose, and rationale of these IM's and the directions issued by MMS Director Bettenberg in his October 16, 1987, Remand Order. Appellant claims that the Deputy State Director's Decision assumes, without analysis, that if incidentally flared casinghead gas is ever captured, it must have been economic to do so at the time of well completion. Appellant claims this assumption is inconsistent with both the IM's and the decisions of this Board.

The Office of the Solicitor has not entered an appearance in this case.

In the April 25, 1994, Decision of the ADM for Mineral Resources, Vernal District Office, the ADM quoted the following language from IM No. 87-652, and determined subsection B to be applicable:

> A. No avoidable loss has occurred and no assessment shall result if:
>
> > 1. The gas was being captured on or before the next day following the expiration date of the initial authorized test period in NTL-4A, i.e., 30 days or 50 [million cubic feet (MMcf)], whichever occurs first, unless a longer test period was approved by the authorized officer (AO); or
> >
> > 2. An application to continue venting or flaring produced natural gas as uneconomic was received on or before the expiration date of the initial authorized test period and was approved, or
> >
> > 3. A plan was submitted on or before the expiration date of the initial authorized test period to eliminate the venting or flaring of gas within one year of the plan's submittal date, and the commitment to do so was honored timely.
>
> B. An avoidable loss has occurred where an operator did not timely satisfy any of the above criteria, <u>but later captures the produced gas</u>. The resultant assessment shall be based on the following:
>
> > As appropriate to the timeframe during which the avoidable loss occurred, full value after the expiration date of the initial authorized test period through October 21, 1984, and royalty value thereafter, to be terminated at any time after the expiration date of the initial authorized test period that the gas is captured.

(ADM Decision at 2.)

The ADM further stated: "There is additional policy established by the Instruction Memorandum, however, it is not pertinent to this case and thus need not be identified."

In reviewing this appeal, we find that the additional policy guidance is highly relevant. As stated in IM No. 87-652:

> The feasibility of capturing gas at any point shall be based on the economics of the operator's total operation on the lease, unitized area, or communitized tract rather than on the total production of the well or wells from which the gas is being vented or flared or only on the gas production from such well(s), i.e., one must consider not only the value of the gas being vented or flared, but also the value of the liquefiable hydrocarbons entrained in the vented or flared wet gas stream, and the oil or other gas which is being captured and sold from that lease, unitized area or communitized tract.

The IM No. 87-652 further states, in pertinent part:

> [I]t should be kept in mind that what is determined to be economically feasible at a given point in time may not be economically viable at a later point. Thus, where an operator continues to vent or flare gas, even though it is being assessed for such loss, a continuation of such practice may be approved later without the operator incurring any further obligation if the authorized officer subsequently determines that it is then no longer economically feasible to capture the gas. It also is probable that there will be some instances where the venting or flaring of gas has been or will be approved because the economics at that time did not warrant its capture but where, due to changed circumstances, it becomes economic to do so at a later date.

Id. at 8.

We find that the above provision embodies the situation in which Appellant found itself. Changing conditions caused Mountain Fuel to agree to begin purchasing casinghead gas from Appellant's wells in November 1983. The IM No. 87-652 recognizes that economic circumstances change and that capturing gas may be uneconomic during one period but economic at a subsequent time.

Finally, the IM places the burden on BLM as much as on the operator to determine, based on monthly reports, whether the vented natural gas was of an economic or uneconomic amount, with the balance of responsibility on BLM when the amounts reported reflected the venting of an uneconomic amount. The IM No. 87-652 thus provides:

> In most, if not all cases of unauthorized venting or flaring, operators have reported and continue to report monthly the volumes of gas being vented or flared. In many instances, however, no action was taken to compel compliance with the applicable requirements until months or even years after the onset of the unauthorized venting or flaring. Thus, when it

> would have been uneconomic to capture the gas as of the critical point in time, the balance weighs on the [BLM's] failure to react timely to the monthly reports, rather than on the operator's failure to seek a timely approval to continue venting or flaring as uneconomic, since no economic loss has been suffered. The balance weighs on the operator's failure, however, when it would have been economic to capture the gas at the critical time.

Id. at 8.

It is therefore clear from the IM that economic and other data must be considered in determining whether vented gas is subject to capture. It is also clear that, as Maxus contends, there was no analysis of the engineering, geologic, and economic data it submitted to BLM.

After the Utah BLM Office received the October 16, 1987, Remand Decision from the MMS, the Vernal District Office issued an April 12, 1993, letter to Appellant stating that in order to finalize its findings, it wanted IM No. 87-652 "application" information for two of the five leases in issue (U-017992 and U-020252-A). No information was requested for the other leases subject to this appeal. Appellant's July 1, 1993, response to the BLM request nevertheless included information about all of the leases. (Ex. 2 to Ex. A to SOR.) Maxus provided specific responses to the BLM inquiries with respect to the Pariette Bench #14-5 Well on Lease U-017992 and the Allen Federal Wells on Lease U-020252-A, followed by an explanation of why it was uneconomic to capture casinghead gas within the Monument Butte area, which encompassed all five of the leases. This information was not considered by the ADM's Decision nor the State Director Decision. See Deputy State Director's Decision at 2.

[1] This Board has previously considered appeals from BLM decisions directing payment for natural gas flared without prior authorization. In Ladd Petroleum Corp., 107 IBLA 5 (1989), we set aside and remanded a BLM decision because BLM conclusively presumed, as here, that gas flared without prior authorization was avoidably lost, and hence, that compensation was due to the lessor. Ladd was given no real opportunity to show that the gas was not marketable when flared. In Ladd, we noted that in 1987, BLM altered its absolute requirement for prior approval of flaring previously set out in Notice to Lessees (NTL)-4A. We stated in Ladd:

> On August 17, 1987, * * * the Director of BLM issued Instruction Memorandum (I.M.) No. 87-652 concerning BLM's policy for avoidably lost gas on onshore Federal and Indian oil and gas leases. I.M. No. 87-652, which applies to both past and future determinations of avoidably lost gas, requires that, when no application to flare gas has been submitted by an operator after the expiration date of the initial authorized test period (30 days or 50 MMcf, whichever occurs first), BLM must notify the

> operator that it has 60 days in which to submit an application to justify its position that it was uneconomic to capture gas both at the time of application and as of the expiration date of the initial authorized test period. Id. at 5.

Id. at 7-8.

Similarly, in Maxus Exploration Co., 122 IBLA 190 (1993), a case arising from BLM determinations following the same audit addressed herein, we noted that at one time there was a conflict in the regulations governing the administration of operations generating avoidably lost gas. In that case, we reviewed the Supplementary Information published with rulemaking when 30 C.F.R. § 206.100 (1987) was promulgated, noting that regulations published by BLM in 1984 were inconsistent with MMS rules on the subject, BLM requiring payment of royalty value for avoidably lost gas, while MMS required full value compensation. Id. at 194; see 52 Fed. Reg. 3796, 3797 (Feb. 6, 1987). We further noted in Maxus, supra, that the rulemaking adopted the rule taken by BLM, providing:

> The amended rule provides that the lessee is obligated to prevent the waste of Federal and Indian onshore oil or gas production in accordance with BLM regulations. The determination of what constitutes waste is the responsibility of BLM, under its operational regulations. * * * This final rule clarifies all existing production value directives regarding wasted or avoidably lost onshore oil or gas production contained in various Secretarial, MMS, and U.S. Geological Survey Conservation Division (Now BLM, Onshore Operations Division) directives, regulations, and NTL's (Notice to Lessees) issued prior to and after the effective date of this rulemaking. * * * BLM, not MMS, is the agency within the Department of the Interior to which the Secretary has delegated the authority to establish substantive regulations governing lease operations and remedies for failure by lessees to comply with its regulations.

Id. at 194-95; 52 Fed. Reg. 3797 (Feb. 6, 1987). It is, therefore, to those BLM regulations we must look to determine whether BLM properly evaluated the data submitted by Maxus. The pertinent BLM regulation provides in relevant part that

> [a] [sic] operator shall be liable for royalty payments on * * * gas lost or wasted * * * when such loss or waste is due to negligence on the part of the operator of such lease, or due to the failure of the operator to comply with any regulation, order or citation issued pursuant to this part.

43 C.F.R. § 3162.7-1(d).

As there is no implication in the record or suggestion by BLM that there has been negligent conduct supporting the assessment made in this case, the BLM determination that there was avoidable loss of gas rests on the determination that there was a violation of BLM regulations. The Deputy State Director's Decision, after indicating that the procedural review under IM No. 92-91 would be no different than under IM No. 87-652, stated:

> Under IM 92-91, where the operator fails to obtain prior approval to vent gas, but later captures the gas for sales, the volume of gas vented from the end of the initial 30 day test period until the time of capture is considered avoidably lost, <u>without regard to the economic circumstances</u>.

(Decision at 2 (emphasis supplied).) The applicable IM No. 87-652, and its successor IM No. 92-91, required BLM to relax the NTL-4A requirement that economic factors can only be considered when there has been a prior application to vent or flare gas. The BLM nevertheless applied the pre-1987 rule that any gas vented must be paid for, regardless whether the action taken would have been economic or not, in the absence of a prior application. <u>Maxus</u>, <u>supra</u>, at 195, determined that "economic considerations are always entitled to consideration on the merits." The economic evidence presented by Appellant regarding the casinghead gas vented from the wells within the five leases should have been considered.

[2] The proper application of IM No. 87-652, and its successor IM No. 92-91 (which BLM states does not change prior policy), requires BLM to evaluate whether, if an application to flare gas had been made for oil wells produced by the lessee prior to flaring, the application would have been entitled to approval on the merits. <u>Maxus</u>, <u>supra</u>, at 198. In <u>Ladd Petroleum Corp.</u>, <u>supra</u>, we considered both IM No. 87-652 and NTL-4A. Concluding that NTL-4A had been properly issued under authority provided by Departmental regulations, we found that the IM permitted BLM to consider economic considerations when deciding whether venting gas was justified, regardless whether a prior application to allow venting had been submitted prior to the venting. This change was considered to be beneficial to lessees. In <u>Ladd</u>, <u>supra</u>, we allowed the lessee the benefit of the amended notice, even though the amendment by the 1987 IM had occurred after the events giving rise to the appeal.

In this case, we also find that Maxus is entitled to consideration of evidence that it was economically necessary to vent or flare gas from the wells in the five leases under consideration. Maxus has properly submitted information to BLM to show that conditions at the time of venting required that such venting be allowed, even though no application to vent or flare had been submitted when the venting exceeded the generally allowed initial maximum amounts. The ADM and the Deputy State Director have chosen not to consider that evidence. On the record before us, therefore, the BLM determination that the Monument Butte operation avoidably lost gas in the amount of 324,323 Mcf is set aside.

[3] As noted above, BLM's April 25, 1994, Decision stated that Maxus must pay the United States for the full value of any vented gas ultimately

determined to have been avoidably lost from 1981 through 1983. Although the Deputy State Director's June 27, 1994, Decision stated that royalty value was due on the avoidably lost gas, it did not disavow the full value basis of the earlier decision. We hold that royalty value is the proper basis, because 43 C.F.R. § 3162.7-1(d), issued in October 1984, changed Departmental policy to limit compensation for avoidably lost gas to the royalty value of the vented gas. See Conoco, Inc., 115 IBLA 105, 106 (1990). Because the 1984 regulation changed the prior policy, which had been to assess vented gas at full value, affected lessees who would benefit by the amended rule are allowed the benefit of the change. Mobil Exploration, supra, at 79.

We also gave retroactive application to policy changes in the administration of oil and gas royalty payments involving vented gas in Ladd Petroleum Corp., supra, at 5. In the past, this Board has applied an amended version of a regulation to a pending matter if to do so would benefit the affected party, and if there were no countervailing public policy reasons or intervening rights. James E. Strong, 45 IBLA 386 (1980). The rationale for such an action is equally appropriate here where BLM has indicated a change in its policy regarding the application of NTL-4A concerning avoidably lost gas which would benefit Appellant, and there are no countervailing regulations, public policy considerations, or intervening rights. See Somont Oil Co., 91 IBLA 137 (1986). On the record before us, we find that the application of 43 C.F.R. § 3162.7-1(d) will not adversely affect intervening rights or prejudice the interests of the United States, and is not in derogation of prior law, but is rather a proper implementation of existing law after amendment.

To the extent BLM's June 27, 1994, Decision affirms full value compensation for avoidably lost gas, it is reversed.

[4] Finally, Appellant urges that enforcement of regulations which it claims have been ignored by BLM is barred by the applicable statutes of limitation including inter alia, 28 U.S.C. § 2415(a) (1994). (SOR at 23.) Appellant claims that it properly filed its production reports on a monthly basis and that these reflected the volume of gas which was vented or flared, if any. Id. Maxus claims, therefore, that since the most recent conduct giving rise to this assessment is 11 years old, it is barred by the 6-year statute in 28 U.S.C. § 2415(a) (1994). (SOR at 23.)

The statute cited by Appellant governs civil actions for money damages brought by the United States and does not affect BLM administration of Federal leases. Whether the manner in which the flared gas audit of Appellant's five leases in Utah was conducted was so slow that it would bar recovery in a suit for damages is not within our authority to decide. Alaska Statebank, 111 IBLA 300, 312 (1989); see also Mobil Exploration, supra, at 81. An appeal to this Board is in no sense the commencement of an action for damages. It is the continuation and conclusion of administrative review that began with the 1983 audit of Maxus' five oil and gas leases in Utah. Our review is conducted on behalf of the Secretary, pursuant to Departmental regulation, and is not a commencement of an action for damages. The purpose of our review is limited to a determination, on the record before us, of whether an assessment against Maxus for avoidably lost gas should be affirmed, and if so, how compensation due the United States should be calculated. See 43 C.F.R. § 4.1. We do not hold that there are no limits on the time that may be taken in administrative review, but only that, in this case, there has been no showing that any limit on such review set by law has been infringed.

Accordingly, pursuant to the authority delegated to the Board of Land Appeals by the Secretary of the Interior, 43 C.F.R. § 4.1, the Decision appealed from is set aside in part, reversed in part, and the case file remanded to the BLM Utah State Director for a determination, based upon information of record submitted by Appellant, whether vented gas from wells within the five Utah leases held by Appellant from 1978 through 1983 was avoidably lost, and should thus be the subject of royalty compensation to the United States.

James P. Terry
Administrative Judge

I concur:

Will A. Irwin
Administrative Judge